Bird's Eye View of the Cash Flow Statement

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Dave

0:00

Alright folks, welcome to Investing for Beginners Podcast. Today Andrew and I are going to take a bird's eye view look at the cash flow statement. So last week we talked about the income statement. This will be a continuation of said conversation. So, without any further ado, let's go ahead and dive in Andrew. So let's talk about why do we care about the cash flow statement?

Andrew

0:21

I guess the simplest way I would try to explain that is companies have to report what their profits and losses are. And that helps them to pay taxes. But what your profits or losses are in any given year, is different from how the cash actually runs through the business from year to year. And that sounds kind of weird, right? Because it's like, well, don't you just have money that comes in and money comes out? And that's your profit? And the answer is yes, and no, because there are, I guess, for lack of better word accounting reasons to have the profit and loss is different from what the actual cash situation of a businesses, and they do make sense when you start to kind of unpack those, and we don't have to necessarily unpack them super in depth.

But the two biggest that come to my mind are depreciation, and amortization, and then accounts payable and some of those things. So maybe we could start, they're just like super surface level of like, why those make the cash flow statement, the income statement, not line up,

Dave

1:31

right? When we started with depreciation, and amortization, those are what you would consider non cash expenses, that the easiest way to describe them is when you think about when you buy a house, you put a whole bunch of money down, and then you make payments on that house until you own it. And in essence, that's what a business does when it built a factory, for example.

And even though there is money going out, it may not necessarily go all out at once, or it could go out and in spurts. And so accountants they will depreciate that value over a period of time to help account for the money going in and out of the business. Even though they may on paper say that they paid a million dollars, for example, for the factory, they won't probably pay all that cash upfront, or they could and then they'll depreciate the value over a period of time. And so the income statement may look different from the cash flow statement just because of those two particular line items. amortization and depreciation are similar terms, in that it just depends on how they're accounted for. With the accountants.

Typically, depreciation is associated with like things like buildings, property, plant equipment, things of that nature, where amortization is generally more air quote intangibles like software or design or something along those lines. But it's, it's treated the same way in accounting. So those two terms are probably most, I guess, similar. Do you want to take a stab at accounts payable?

Andrew

3:03

Sure. So when two big businesses interact with each other, let's say like, what would be a good example, about Walmart and the people that they buy from, or Costco and the people that they buy from? Yeah, perfect. So when a big food company and Costco are dealing with each other, and this big food company has given them huge shipments of food that Costco is turning around and selling, they're not going up to Costco and Costco has given them a debit card and swiping for those goods. It's just a lot of money that's transferring hands.

And so the way that kind of behind the scenes some of that stuff will work is you can have this kind of like IOU, and we're gonna pay you later kind of a thing. And there's all these reasons behind that. So when you start to deal with all of those with lots and lots of different businesses, the timing of when you actually get the cash versus when you get the inventory can be different. And so that's why we have to account like if you're a Costco, you have to account for the profit and the loss once you sell the item, because you paid a certain amount for the item, and then you receive cash from the customer.

And then that's your profit, but you might not necessarily need to give the food company that provided the item, you might not have to give them the cash now, maybe it's in 90 days once you've accumulated a bunch of sales. So that's that's kind of why and why you'll see as another big example of why how the cash actually moves between businesses might be different from what's your profit and loss. Yeah, exactly.

Dave

4:42

And I think something that's important to think about that when you think about those kinds of ideas, it really does affect the cash flow of the business and it affects the money going in and out of the business. And that's why it's important to understand a terminology like an accounts payable because you know, the Business takes the product, they start selling it and start generating revenue, but they don't pay the business that they bought the product from, until their contract is due.

So in the restaurant businesses, it's very common to buy food on a 30 day basically window. So you order the food on day one, and then you don't pay for it until day 31. And so you can start generating revenue from those sales, but then you have a big bill due on day 31. So it's part of managing the cash that you bring in versus when the cash goes out. And like Andrew said, it's all about the timing of how those different things work. And we have to remember that when we're looking at these types of statements, they're generally cumulative.

So a cash flow statement and income statement are things that you look at over a 90 day period. And so it's, it's a longer period where the balance sheet is a snapshot in one day. So it can be the timing of everything could be a little bit different. That's why sometimes, when you try to balance everything, or match everything up, it doesn't always match up super evenly. And it can be a little confusing for beginners.

Andrew

6:06

I guess the last thing I would double click on when it comes to that, because I think it's important is, in general, the income statement will be more smoothed out. And the cash flow statement can be very lumpy because of all of the factors that we've described. And so when you think about that, that actually makes sense, because in a way, the profit and loss of a business reflects their true ability to make profits. And that's why the government taxes them on that basis.

And so it does make sense. So when when I'm looking at the cash flow statement, I'm trying to look at the bigger picture. And maybe if there's big swings, and however the cash is moving, I'm trying to adjust for that. So you know, I'll take a, I won't necessarily take one year's cash flow at face value, if you're really digging into this, you want to take a bigger picture look. Whereas with the income statement, it's a lot simpler, there is still depending on the company a lot of fluctuation with that, but it's a lot less. And so you can take one year of income statement, more at face value than one year of cash flow statement. And that's just the reality of it. And it's not like a good or bad. That's just that's just the way the cookie crumbles.

Dave

7:25

Yeah, exactly. And I think that's an important distinction to understand is the differences between the statements and maybe how lumpy they can be because it can be a little discerning you look at the income statement. It's like, Hey, this is as smooth as silk. And then you look at the cash flow statement. And it's like a roller coaster, it's all over the place. And you think, Oh, well, that's not good.

So I think having that kind of bigger, bigger picture view is very important. So let's talk about real quick about kind of the structure of the cash flow statement. And then we can maybe dive into some of the things that we think are important for, for beginners, especially to start to try to pick out perfect

Andrew

Yeah, go ahead.

Dave

8:03

Okay. All right. So the cash flow statement is broken up into three main components, if you will, and they each are fairly intuitive, but if you're not quite sure, so the first section generally is going to be cash generated from operating activities, or cash generated from operations. Again, terminology, we can fluctuate a little bit from company to company. But if we look at, for example, if we look at Apple's cash flow statement, at the bottom of the first section, you have operating activities, and you have cash generated from operating activities. So within that section, you're going to see all the money that would move in and out of the business based on the operations of the business.

So for example, accounts receivable inventories, the depreciation we mentioned earlier, the net income, which is a direct reflection of the money that you see at the bottom of the income statement, so that

number, if you look at the income statement, at the bottom of it, the net income earnings, whichever terminology you want to assign to it, that's gonna be the exact same number that you're going to see at the top of the cash flow statement where it says net income, so that that helps you kind of align the two statements. So after we look at the cash from operations, then we're going to look at the investing activities. And this is going to encompass any money that they might invest in securities, it could also could look at property, plant and equipment or investments, acquisitions, any money that's going to come in and out based on those activities, is going to be an investing activities.

And that's going to be the Cash used and investing activities. And then the final section is financing activities. So this is where you're going to see information regarding dividends, any sort of debt, whether they take on debt, or whether they pay down debt, but repurchase of stock payments, anything along those terminology. That's all going to be under the financing and that would be cash used in financing activities. And those are the three main sections that you want to think about when you're looking at the cash flow statement. Is there anything that I missed you like to add on to,

Andrew

10:02

I don't think he missed anything. I think maybe it should have given the disclaimer like some of our episodes, that I would actually listen to the income statement episode first before trying to tackle this one, because I think if you tackle this one before the bird's eye view income statement, you'll get lost. So I would start there.

Dave

10:23

Yeah, perfect. All right, so now that we kind of have an understanding of maybe the basic overview of how the cash flow statement is structured, maybe Can we talk about maybe some specifics or kind of, I guess, digging a little deeper on some of the items that we pay attention to, and I think would be beneficial for beginners to start to look

Andrew

10:42

at? Yeah, I'd like to take a similar approach that we did in the income statement episode. So we're gonna highlight two line items that we feel like bare necessity, make sure you understand this part of the cash flow statement. And then we're going to take three companies and use their actual cash flow statements to kind

of teach these concepts. So again, we're going to look at Apple, Starbucks and Netflix, as businesses I think a lot of people are familiar with.

So the two line items would be cash from operations. Let's so let's start there, that would be the first one cash from operations. So to Dave's point, these are all of the things that deal with the operations of the business. So if we're talking about Apple, this can be anything related to what drives their operations. So ask yourself what drives the operations are apple? Well, they sell iPhones, they also sell services on their app store. These are the platform or developers can make apps and people can download and make purchases on them.

So those if those are two biggest operations that we identified in the income statement in the last episode, cash that relates to the operations of that are going to be in this section, that's a great place to start when you're trying to think of what's the free cash flow of the business? Or what's this business's ability to generate free cash flow, I look at Netflix as an example of why that's important, and why it might be different from the profit and loss that you host as a business, because a lot of Netflix's assets are very long term.

So again, if you think about what are some of the biggest drivers to Netflix, and why? Why do people find that value? Valuable? It shows like Squig game, it shows like Stranger Things, these blockbuster hit TV shows that people will binge through that they've been working on for years and years and years of great all the seasons give people a reason to subscribe. So because it's so long term in nature, the profit and loss looks a lot different from the cash flow statement. And that's why it would be important to look at that part of it. What would you say about the cash from operations park because it can get pretty weedy, like a lot of weeds. But it is very important. It's critically

Dave

13:07

important. And I think the thing that I like about this particular section is it really helps narrow down where the money goes in and out for the business and really aware, you can see how well they manage the business, like the operations of the business, whether it's things like inventories, depending on the business, something like an inventory line item might be very large. For example, if you look at Walmart's versus Netflix, those numbers are going to be vastly different because of the nature of the type of business that they operate in.

And so just looking at that particular line item helps you understand how management manages the inventory of Walmart, because that's very critical for them. Because if you think about it, they want to have

the right amount of stuff on the shelves to sell to people. But they don't want to have too much that they're stuck with it. And that was something that target ran into, and a lot of companies ran into trouble kind of coming out of the pandemic is there was so much demand built up for all these things that some of these companies went out and went crazy and bought tons of inventory of things. And then all of a sudden the demand dried up like just poof. And then the company is stuck with all these TVs, for example.

And what are we going to do with these? Well, they have to mark them down. And that impacts the cash flow of the business. Because if you pay $200 for TV, and now you only sell it for 100 Well, you lost $100 Well, that's money you don't bring in now. So that's that's a loss and profit. And so that's why understanding maybe the ins and outs of some of these numbers, and as a beginner at first, I would just start with one thing and think about what that business does.

And think about one thing in this section that may impact the business and try to understand that a little bit better. If you start diving into every single line item going piece by piece by piece, you'll drive yourself nuts because some of this stuff is esoteric is not the right word for it. But it can be a little confusing to try to really dive into share based compensation, for example, that's a landmine, I would stay away from until you understand financial statements a lot better. But something like inventories is something I think everybody can understand.

And it can impact different companies differently. And so just understanding that accounts receivable is kind of the opposite of accounts payable. And so just understanding that line item, depending on the business may have a big impact on that business. And so something like a company like Netflix, for example, accounts receivable has a different impact than it would on Walmart. So those are kinds of things that you want to start to get your head around, and then that all underneath, it'll help you understand cash flow from operations a little bit better.

Andrew

15:45

So let's unpack that, because that's a perfect place to start. And we can do that with these three companies to focus on one part of the cash from operating activities. And that's what makes it interesting to like, you highlighted the difference between Walmart, and their inventory and Netflix. Netflix is inventory is looking at their cash flow statement. Now it's non existent, they don't have a sense because it's a digital subscription. Right. But their additions to content assets, which are the cost to produce a TV show is a huge, it was minus 16. Point 8 billion in 2022.

So you see how like two completely different businesses between Walmart's gonna have a lot, depending on what year you're looking at, they could have added to inventory a lot, versus Netflix, who had zero inventory. But we're able to compare these two very different businesses on a very apples to apples basis, because to your point they've, we can see how a company has managed their cash flows. And a lot of that, like you said, has to do with kind of a in a way a capital allocation, but just how they're thinking about their business, how they're investing how they're spending money in the business. And it might not make an impact to the profit and loss immediately. But it certainly drives the impact of the business over the long term.

Right. So the take the example of kind of over investing in inventory, like Target did, that did not when they spent a lot of cash on inventory that did not affect their profit and losses that year. But if all that cash they spend the inventory ends up being losses they have to take that's going to play out in future years. And so the whole pandemic, huge demand and then fade away, I think was really instructive.

And I'm sure we'll see. So many business lessons learned from these things, because you did have very contrasting situations where for some companies, they double down on inventory, and it was a huge, huge win for them, like they grew at crazy amounts, they still have great demand. I think a company like watsco distributor, that is a good example of that. They invested inventory hugely. And it actually was a great thing for their business. And they've seen huge gains and profits. So as it comes to the cash flow statement, maybe the next point I would make and then we'll we'll get we'll get to the practical kind of takeaway that I said we were going to do is that there's not a black and white thing.

So if you see huge increases or decreases in certain cash category, I would not call that bad or good. I would say it depends on how you perceive the way they're doing the cache. So that makes it very gray area ish, where the bank statements kind of a lot nicer, because you can just see the history that profit. But you would argue a lot of the a lot of potential is there.

Because of this, there's a lot of opportunity in digging into the cash flow statement, because some of that stuff, the way you interpret it can be subjective. And by finding companies that are managing their cash flow as well, that can go a long way towards finding a good investment.

Dave

19:07

It absolutely can. And I think one thing that you want to understand when you're starting to start to dig into the cash flow statement is it connects directly to the balance sheet. And without going into a lot of nitty gritty, because we'll do that in the next episode when we talk about the balance sheet. The cash flow

statement will give you indications of how much money they're spending on these particular items. But the balance sheet will show you how much they have sitting around if you will. And so when you think about inventory, again, going back to the Walmart Costco kind of idea, when they buy that inventory, it sits on their balance sheet as an asset because they haven't sold it yet.

And when they sell it then they receive money for that. And so the cash flow statement will show you how much they're spending on inventory and so you can kind of use both of them to see how well the company manages Is there inventory, and you can look at overwhelmed. Again, this is, you know, year by year, it's not going to tell you much. But if you look at a five or 10 year period, then you'll get a much better indication of how well they're managing the inventory, how much it goes in, and how much it goes out.

And that will help you understand how the company manages their operations from day to day that the cash flow statement is telling you how much they're spending on it, the balance sheet will tell you how much they're sitting on, and how quickly they're turning it and all those kinds of things. That's another conversation for another day. So now that we've kind of understood a little bit of this particular idea, can we maybe start talking a little bit about some practical takeaways from those two? Those two ideas?

Andrew

20:41

Yeah, bring me back, bring me back. All right, let's go back to Apple because Apple's easier. Okay. So with Apple, you have your profit and your loss. And it's pretty straightforward for them. Because people are buying iPhones, they're upgrading every year, every two years, every five years, whatever that is for each person. And you can really easily see that play out every year, when I look at what their inventories are, it's very close to zero. So what the cash flow statement is doing, again, it's not to your point about the balance sheet, it is not saying only what we're spending on inventory, but it's also saying it's also showing you how much cash we're making from the inventory. So think about it, we're, we're buying the components, and we're assembling the iPhone, and that patch that we spent, goes into the balance sheet, and then it sits there, and then it comes back.

Once the customer buys it, they give us the cash, the cash comes back to the cash flow statement. If our cash changes and cash from inventory does not change much, we basically sold out of everything that we invested in. And you can see for Apple, that's been the case. And the reason I say that is because there's one and a half billion and then minus two and a half, but their cash from operations is 122 billion 104 billion. So you look at a billion dollars, and then $100 billion dollars, that's degrees degrees of order of magnitude of difference. So they're basically not heavily investing in inventory too much, or they're not like pulling back the

reins too much in inventory. They're basically selling out of everything that they're investing into it, you can look at that as a good thing. Or you can look at it as they're being conservative. However you want to look at it, I think it's instructive and kind of seen that where Walmart is very inventory heavy, Apple does not appear to be based on looking at the inventories. And that's one of the takeaways I would take away from looking at the inventories on Apple's cash flow statement. Yeah,

Dave

22:49

yeah. And if you look at Starbucks, it's similar, the previous two years, it was very minimal, this last year was a little bit higher. But again, you're gonna see fluctuations from year to year. And it depends on what's going on with the business and whatnot. So instead of rushing to judgment on a larger number for one year, over the previous two years, it'd be better to look back over a longer period and see if it's out of the norm for them. Or if that's something that is normal from time to time, like every three years, they buy a whole bunch of inventory, and then they sit on it, because coffee is not going to go bad as quickly as something else.

And the popularity of French roast is not going to dwindle from now until a few years from now. So that could have a bearing on some of those things. And of course, Netflix has no inventory. So we don't have to worry about that one. So those are some you know, I think Andrews example with with Apple is a great way to kind of think about inventory and the impact it can have on the cash flow of the business and the cash from operations. And I think kind of, I guess, moving from there, where would investors start to kind of move? Once we've kind of understand this? Can we start maybe talking a little bit about the famous free cash flow term?

Andrew

24:00

Sure. So again, there's the different line items that deal with the operations. And in general, yes, it fluctuates from year to year. But in general, it's kind of trying to tell you what's the one year picture of how the cash has moved, and that's why it's operating activities. But then, as we've discussed, there's also a longer term uses of cash in the business and that's they're investing in the future, right? So one of those is what's called capex or capital expenditures, or in the cash flow statement. Apple's talking about payments for acquisition of property, plant and equipment.

And those are kind of like Dave was saying like a factory or a plant places for years and years will produce products are produced revenue for the company. And every business can have a different definition of that one that could be kind of simple to think about would be like an office building. Being mean that I think

companies in general have different policies on whether they rent an office or buy an office. But it's not uncommon for a company to have at least one office that they own. And they use that as headquarters. And so that's one example of property, plant and equipment, or they might buy the land, they might buy the building, or do the construction on the building. And that's going to last them for 1020 30 years. And so that's why the cash deals with that because as CapEx and so we use that first number that we focused on cash from operations, we subtract the capex, that gives us the free cash flow.

And that's where a lot of nerdy Wall Street types like us like to start a valuation at, because again, it gives us the true picture of the cash flow of the business, which tells us how they kind of invest and how they manage the actual cash. And, by the way, it tells you what's the cash flow available to shareholders, as owners of a business, we want to get that money returned to us eventually. And so when they have that free cash flow, they have that available every year to give back in dividends or buybacks or to grow the business. Whereas a company's profits may or may not go to you, depending on how a company's managing those profits, if that makes sense.

Dave

26:22

Yeah, it totally does. And I think one thing that people should understand the term free cash flow is, it's a very, very common term. And the calculation for it is very simple. And it's really the base that you can use to make, start making any sort of adjustments that you feel like you need to make for that business. But if you don't understand what the free cash flow is, and how you determine it, you can start going down a rabbit hole of all these different terminologies and throwing all this stuff on there. And it can get really confusing. And so free cash flow is always kind of the home base. And then you can start working off of that, depending on how in depth you want to get. And also how in depth, you want to understand the different impacts that it can have on the free cash flow of the business.

Because the operations of the business is obviously very critical. But then kind of the, to Andrew's point, the capital allocation, or how the company invests that free cash flow is also very, very important, not only to the business, but also to us as shareholders, because if they poorly allocate that money, then that means that that's less money for us. And so that's part of a way you can analyze a CEO is by looking at how they allocate that money. And I guess maybe we can talk a little bit about the some of the capital allocation decisions that a they can make, and what we can find in the cash flow statement that we can kind of figure from that. Sure. Alright, so let's chat about capital allocation quickly.

So capital allocation really comes down to what does the CEO want to do to try to improve the business. And they have, I guess, five different ways that they can do that. Number one is they can reinvest in the business. And number two is they can buy another business or act to acquire a business or a part of the business. They can also pay a dividend, they can also do share buybacks, and they can also reinvest in the business. And so you have these different methods and ways that they can go about doing that. And how well a CEO reinvest that money goes a long ways towards how successful that business is.

Because it's not just enough to generate profit or free cash flow from the operations of the business, they also have to allocate that money wisely. And one of the things that sets Warren Buffett apart from other CEOs is his capital allocation skills, he's very, very good at deciding what's going to be best for the business and for the shareholders. Because again, it all comes back to us. And so if we're not investing in the business, then they shouldn't give us money back. But because we are, they should figure out a way to do what's best for us and the business, not for them personally.

And so there's some ways that you can see some of the decisions that a CEO may make, what kind of capital allocation, how they want to spend that extra money, if you will, after the operations because like Andrew was talking about free cash flow really comes back to money that's left over after they operate the business and they reinvest in the business. And so by looking at some light other line items in the cash flow statement, for example, you can see if a company pays a dividend like Starbucks and Apple do, you can see in the cash flow statement, there is a line item that talks about the dividends paid. So that's the money that they pay out for dividends. And so you can see how the company does that. You can also see if they buy back shares, there's common share repurchases a line item in there. that will see that you can see how much they're buying back of shares.

For example, you can also see acquisitions, if a company is acquiring a lot of other businesses, it will be there in the Investing section of the Cash Flow Statement. And so the dividends and the common stock would be under the financing decisions. And as well as the debt, so any debt that the company takes on, you're gonna see that as money coming into the company, any debt repayments is going to be cashed, they paid out, they paid off some of the debt just like we do for our mortgage. So those are some of the items that you will see the help you kind of give you at least a sense of what the company is allocating towards their different allocations of investments and things of that nature.

And so it's not critical that you look at those and understand them as intimately as may say, capex or inventory. But it's certainly helpful to see if they're growing the dividend, if they're growing the share repurchases, and how much are they actually spending on that. And I guess another item to think about with

that is, if they're paying out more dividends than they have free cash flow, that's also a capital allocation decision. That means the company is having to take on money from other places, ie debt to pay that dividend. And that's not sustainable. And so those are things that you can take into consideration when you're looking at that section of the Cash Flow Statement as well,

Andrew

31:22

once a great point, is very great point. And so the free cash flow is where I think a lot of people focus attention on because that tells you in theory, how much cash a business can allocate. And then those line items will tell you exactly how that cash is being allocated right now, in any given year.

So it is a good place to check. Is management actually doing what they're saying? And are they doing something that might be unsustainable not to pick on Starbucks, but one of the things that concerned me when I looked at their cash flow statement was that exact thing where they had a ton of buybacks, which not necessarily a bad thing, but then their debt was ballooning. And you could see that by looking at the long term picture of their cash flow statement.

Because like, wow, they, they bought back a lot of stock. Alright, that's great for shareholders, oh, they added a ton of debt that might not be great for shareholders. So they borrowed a lot of money to paper to buy back stock is that best for long term of the business? That's where you can if you see things like that you can use it as a cue that hey, maybe I need to look deeper here. What's management really doing here?

Dave

32:35

Yeah, exactly. That's a great takeaway. And that's, those are some insights that you can gather from looking at the cash flow statement, like anything else, as you get more experienced using these statements, you'll get better at picking out things and finding things that are important for each particular company. Some companies are going to acquire, for example, some companies are going to acquire a lot of businesses and others aren't. And so some of the you see that might not, then it's not going to be as important to focus on that particular area.

But others that do that could be far more important. And some are going to be more I guess, occasional acquirers. Like they'll find a great business that they'll allocate money to once in a while, and others are going to do it more on a regular basis. But again, you have to take a business by business to kind of get an

overview of how all that works. But like Andrew, going back to what Andrew said, in theory, the cashflow is the money that they can use for those things.

So it's important to understand how much they have and what they're allocating it to, for those piti or items. Because, like Andrew was saying, with Starbucks, you don't want to see ballooning debt, as they continue to try to pay some of these things, because it's not sustainable, because at some point, you won't be able to borrow enough because you can't pay it all back. And that's where it can come. That's where problems can come into play.

Andrew

33:49

Yeah, just take that one step further. Because like I was trying to say at the beginning, nothing's good or bad. It's just how you interpret it. As far as the cash flow statement goes, not making any other big claims here, the ballooning debt might actually be a great thing, if they are reinvesting it in the business. With Starbucks case, when you don't see as much reinvestment as you see buybacks.

That's where the alarm bells start coming. So I just want to make sure we're thinking in the same direction trying to implement this the good mental models to have I look at cash flow statements a lot when I'm doing my evaluation. And so I guess I'm pretty passionate about how to look at it in the right way. The other thing I would say is, I would try to smooth out some of these some of these big kind of like changes in working capital, I like to smooth that out over a longer time period. Because again, it can be so up and down. And I also recommend including acquisition, acquisitions in your quote unquote free cash flow, because a lot of people actually don't do that. But you're basically ignoring how they're growing the business.

And so, you know, we can assume that the quote unquote free Cash flow is being used properly. But if it's all going acquisition, then those acquisitions are not moving the needle in a company's income statement. And you can uncover that through ROIC. But sometimes you can also visually see it, if you just consider it as an important line item as well. So I guess those are all like seeds I would plant in, if you're diving down the difficult path of looking at financial statements, trying to keep these big points in mind, what else would you kind of add? As far as something to keep in mind when looking at this maybe part of the thoughts?

Dave

35:35

I think you covered her really well, I think if you understand the base, and you take into consideration what Andrew was suggesting, with acquisitions, you're really going to cover yourself from, I guess, over valuing the business based on what you think is going to happen with the business. And one of the things that you can run into problems with cash flow statements is, there are a million adjustments that people can do make when they're thinking about cash flow statements.

And I think it's important to really understand what the cash flow statement is trying to tell you, and have a base of what you think the cash flow or what the value of the cash flow is, and make sure you're consistent with it. In other words, if you do an adjustment, if you I hate to keep saying adjustment for acquisitions, but if you go beyond the air, quote, a textbook, calculation for key free cash flow, which is cash from operations, less capex, or property, plant and equipment, if you make something a part of your cash flow is removing acquisitions, like from the cash flow, which I agree with Andrew is very, very important. If you do that, you got to do that with every company. Because if you don't, then if you come across a company that if you're just doing it like the Oh, this one does a lot and this one doesn't.

You're gonna we it could we to miss judgments on free cash flow. And when you're doing valuations that could we do further miscalculations of how much the company is actually worth, because the company may have done really great acquisitions two or three years ago, or even four years ago that you don't see in the three year incomes or cash flow statement on the 2022, Apple's 10k. And if you don't see that, and you don't account for that, that could lead to problems with what you think the company's worth and cause you to overpay for the company.

And we don't want anybody to do that. And so it's really important to remain consistent. If you have rules. If you have ideas of how you want things to be, then I would strongly encourage you to to remain consistent to that. And so using the free cash flow that we described today, less acquisitions, I think is awesome. And that's something that I'm going to start doing because I frankly did not do that. But I am going to do that because I think it's you Andrew pointed out, it's a very critical thing to think about. And because I'm going to do it that way, I'm going to do that with every company, whether it's Walmart, whether it's apple, whether it's data dog, whether it's PayPal, it doesn't matter, you just need to make sure you're being consistent with it. That's perfect.

All right, well, with that, we will go ahead and wrap up our conversation on the bird's eye view of the cash flow statement. We threw some jargon at you today. And we know that if you are confused about anything that you talked about today, please check out our website e investing for beginners.com We have a very large search bar that you cannot miss at the top. And if you do not understand inventory as well as you'd like

to or cash flow, or free cash flow or accounts payable, accounts receivable, any of the terminology that we threw at you today, there is an article there that will help explain that in more depth that you will be able to understand this idea better.

And it probably would be a great companion. As you work through your first cash flow statement is to pull up our website, look at the different terminologies you come across it so you can help better understand what it is you're encountering and be able to decipher it better. So again, that's the investing for beginners.com. It's a resource there for you to learn all the stuff that we're talking about today. So without any further ado, I'm gonna go ahead sign us off you guys go out there and invest with a margin of safety emphasis on the safety. Have a great week, and we'll talk to you next week.

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